

Public Hearing: Consultation on RTS on equivalent legal mechanism for unfinished property

EBA Prudential Regulation and Supervisory Policy

Virtual meeting, 11 June 2024



Ground rules for this virtual meeting.

Mic and video off

Please keep yourself muted and the video off while listening.

Questions/comments?

Please use the chat or raise your hand to ask for the floor.

Slides on EBA website

The presentation used today will be made available on the EBA's website after this hearing.

Contents

1 EBA Roadmap on CR mandates under CRR3

2 Legal basis and Scope of the GLs

3 Baseline vs Alternative Approach

4 Questions for consultation

5 Next steps

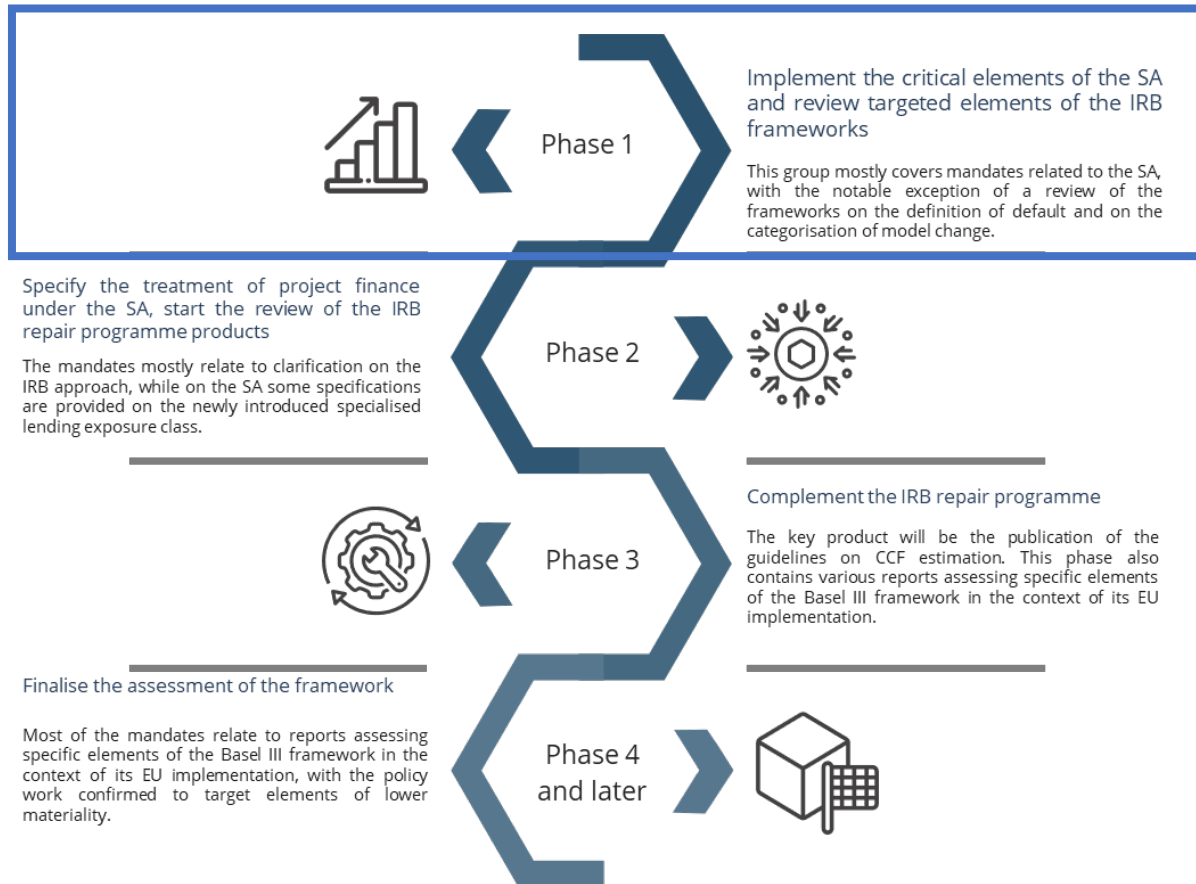
6 Annex



01

EBA Roadmap on CR mandates under CRR3

EBA Roadmap – Overview CR



EBA Roadmap – CR Phase 1

Area	Product	Reg.	Article	Deliverable	Legal deadline
Phase 1					
Credit risk	Report	CRR	506	Report to the Commission on the eligibility and use of policy insurance as credit risk mitigation techniques	0 months after entry into force
Credit risk	ITS	CRR	20(8)	ITS on joint decision process for internal model applications	12 months after entry into force
Credit risk	RTS	CRR	111(8)	RTS on criteria that institutions shall use to assign off-balance-sheet items, constraining factors for UCC and notification process	12 months after entry into force
Credit risk	Guidelines	CRR	123(1)	Guidelines to specify proportionate diversification methods for retail definition	12 months after entry into force
Credit risk	RTS	CRR	124(12)(sub 1)	RTS to specify the term “equivalent legal mechanism” in place to ensure that the property under construction will be finished within a reasonable time frame	12 months after entry into force
Credit risk	Guidelines	CRR	126a(3)	Guidelines specifying the terms substantial cash deposits, appropriate amount of obligor-contributed equity and significant portion of total contracts	12 months after entry into force
Credit risk	Guidelines	CRR	178(7)(sub 1)	Guidelines on the definition of default, in particular for diminished financial obligation	12 months after entry into force





02

Legal Basis and Scope of the RTS

Legal Basis and scope of the RTS

Mandate: Article 124(12)

*EBA shall develop draft regulatory technical standards to specify what constitutes an “**equivalent legal mechanism** in place to ensure that the **property under construction is completed within a reasonable time frame**”, in accordance with Article 124(3)(a)(iii). EBA shall submit those draft regulatory technical standards to the Commission by ... [1 year after entry into force of this amending Regulation].*

Scope of the CP RTS

Applies to residential real estate exposures under construction, built around the **three conditions** of Article 124(12) :

- **Condition 1:** Where a central government, regional government or local authority or a public sector entity involved, exposures to which are treated in accordance with Articles 115(2) and 116(4) of the CRR, respectively, ...
- **Condition 2:** ...has the legal powers and ability to ensure that the property under construction will be finished within a reasonable time frame...
- **Condition 3:** ...and is required to or has committed in a legally binding manner to do so where the construction would otherwise not be finished within a reasonable time frame.



03

Baseline vs Alternative Approach

Baseline and Alternative Approach

Two approaches proposed:

❖ Baseline (main text)

- [Condition 1 changed]: Non-central government, with Counter-guarantee provided by government / assimilated entities
- [Conditions 2 and 3 unchanged]: non-central government has legal power and ability + is required to finish construction in a reasonable time;

❖ Alternative (consultation box):

- Non-central government entity responsible for ensuring the **completion within a reasonable time frame**.
- Private completion guarantees with **safeguards in place**:
 - Mechanism enforced by law in a mandatory manner;
 - Protection provider: institution subject to capital requirements ≈ to banks or insurance
 - minimum level of creditworthiness: RW ≤ **20%**.
 - minimum requirements on the guarantee
 - Wide coverage of the construction risk
 - Minimum standards for guarantees as provided in Article 213 - CRR (adjusted for the specific case)



04

Questions for consultation

Questions for consultation 1/3

Practical cases consideration

Possible drawback of Baseline Approach: **only a few (none?) practical cases** (no central governments providing counter guarantees?)

Q1(a) and Q1(b) practical cases of:

- Central governments or public entities ensuring property completion (CRR original Article 124);
- Entity other than central government ensuring property completion (RTS baseline & alternative approach).

Minimum requirements on the guarantee

Alternative Approach safeguard: **minimum requirements** in terms of **guarantees** (not limited to credit worthiness of developer, but also including construction risk).

Q2: Activation of the **guarantee rights** (legal and practical).

Q4: Alternative mechanisms ensuring recognition of **construction risks** (beyond the real estate developer's financial difficulties).

Questions for consultation 2/3

Minimum Level of creditworthiness

Alternative Approach safeguard: RW (protection provider) \leq **20%**.

Q3: RW of current protection providers of completion guarantees

Scope of application

Scope of application the equivalent legal mechanism: **IPRE and non-IPRE exposures**.

Q5: Unique characteristics of IPRE vs. non-IPRE exposures for differentiated requirements.

Questions for consultation 3/3

Empirical assessment of the effectiveness of the equivalent legal mechanism under the Alternative Approach

Q6: Empirical evidence of sovereign intervention outside Europe for unfinished properties.

Q7: Average time for protection provider to step in and complete construction after developer default.

Q8: Historical average loss rates for developers and completion guarantee providers.

Q9: Empirical data related to:

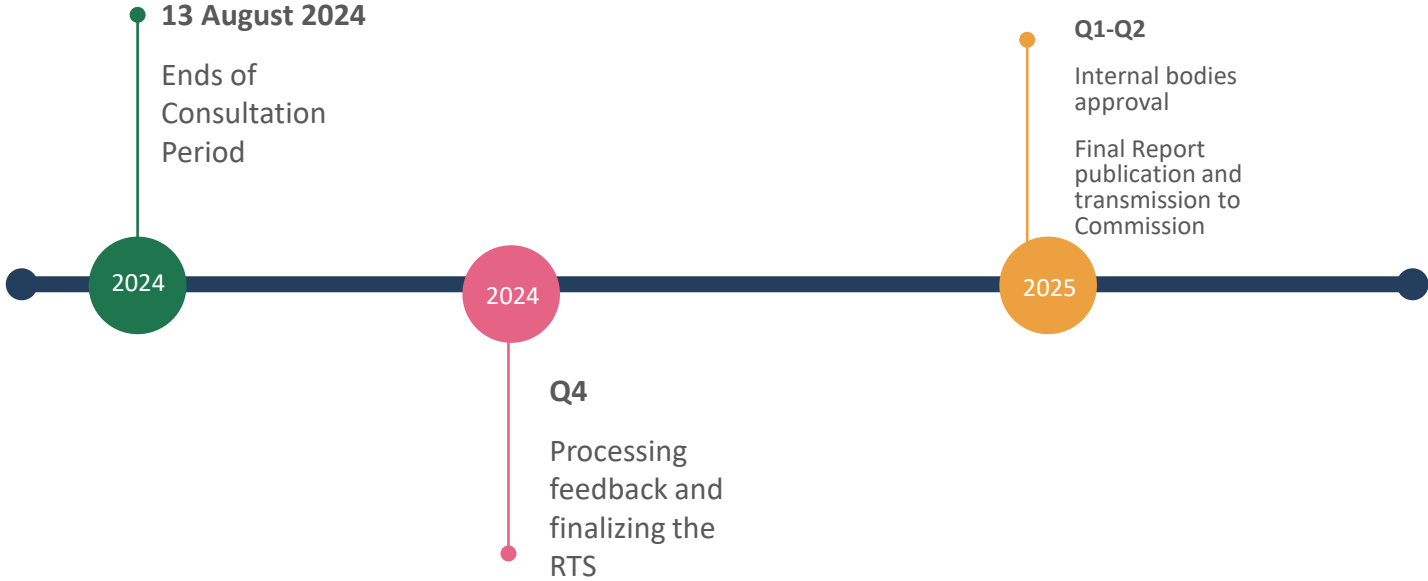
- a) (Number of triggered completion guarantees) / (total number of projects covered by the guarantees)
- b) (Triggered completion guarantees that resulted in completion) / (total number of triggered completion guarantees)
- c) (Triggered completion guarantees transformed into repayment guarantees) / (total number of triggered completion guarantees)
- d) (Cases where protection providers failed to meet obligations due to any deficiency) / (total number of times completion guarantees were granted, specifically in cases where real estate developers defaulted).



05

Next Steps

Next steps

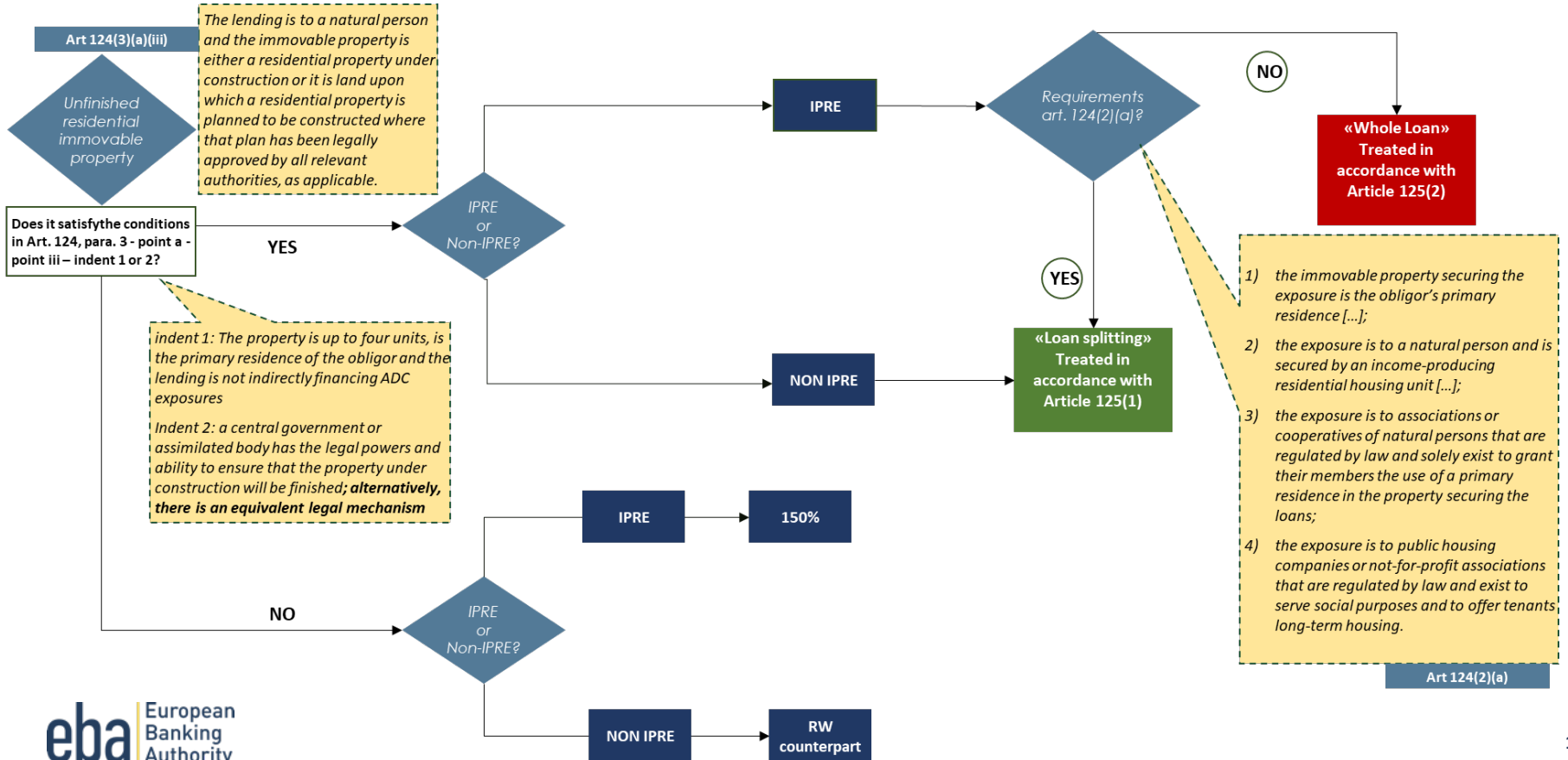




06

Annex

Regulatory Treatment of unfinished RRE





Thank you!



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